

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Kehoe Analyst: Roger Lackey Bill Number: AB 684
Related Bills: See Legislative History Telephone: 845-3627 Amended Date: 06-27-2001
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Authorizes Credit Unions To Engage In Trust Business

SUMMARY

This bill would allow credit unions to engage in trust business.

This analysis will only address the bill as it impacts the Franchise Tax Board.

SUMMARY OF AMENDMENTS

The June 27, 2001, amendments revised the Corporations Code and the Financial Code to allow credit unions to engage in trust business. These amendments are further discussed in the THIS BILL portion of the analysis below.

This is the department's first analysis of the bill.

PURPOSE OF THE BILL

According to the author, the bill's purpose is to extend the authority to engage in trust business to credit unions, thus expanding the services provided by credit unions.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative January 1, 2002.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Federal law provides that trusts are taxed in the same manner as individuals. Income generally is taxed to the trust, if retained by the trust, or to the beneficiary if distributed. Thus, if the fiduciary distributes income to the beneficiary, the trust deducts the distributed income, which then becomes taxable to the beneficiary. Income distributed to beneficiaries retains the same character (capital gain, exempt income, etc.) in the hands of the beneficiary as it had in the hands of the trust. Deductions and credits of trusts are basically the same as those allowed to individuals except that a trust is not allowed a personal exemption and is allowed certain special deductions related to administrative expenses.

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
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<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Department Director

Date

Gerald H. Goldberg

08/01/01

California law generally conforms to federal law with respect to the taxation of trusts and beneficiaries. The taxable income of an estate or trust is computed generally in the same manner as taxable income is for individuals except that certain deductions are allowed for administration, for income paid or set aside by an estate or trust, for income required to be distributed currently, and for certain amounts paid or required to be distributed.

The tax exempt nature of a trustee does not alter the taxation of the trust, the income of the trust, or the beneficiaries of the trust.

Under current state law the Nonprofit Mutual Benefit Corporation Law regulates credit unions. Credit unions may incorporate in this state for the purpose of providing credit, loan, and banking services to its members; however, credit unions are prohibited from transacting trust business. Generally, credit unions are exempt from taxation, except for income generated from an unrelated business. For purposes of this bill, income received by credit unions from a trust business would not be considered unrelated business income and would be exempt from taxation.

THIS BILL

This bill would authorize credit unions to engage in trust business.

This bill would make a number of administrative and technical changes to the Corporations Code and the Financial Code relating to the authorization of trust business for credit unions. These changes would not impact the department and are not discussed.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would not significantly impact the department's programs and operations.

TECHNICAL CONSIDERATIONS

This bill provides that two or more credit unions will be deemed affiliated if they are members of the same "affiliated group" within the meaning of Section 1504 of the Internal Revenue Code. There appears to be confusion regarding this reference. The IRC section requires one corporation to own the stock of another corporation. Credit unions are incorporated under the Mutual Benefit Nonprofit Law. That law does not authorize the issuance of stock. Instead, it authorizes the issuance of memberships. Since no stock exists for or between credit unions, it appears the IRC reference may not be appropriate.

LEGISLATIVE HISTORY

AB 2070 (Kaloogian, 1997/1998) would have allowed foreign (other state or nation) banks to transact trust business in California. The bill failed to pass through the Senate Appropriation Committee.

OTHER STATES' INFORMATION

The laws of *Florida, Illinois, Massachusetts, Michigan, and Minnesota* were reviewed because their tax laws are similar to California's income tax laws.

In these states the services provided by credit unions are limited to savings, checking, and loan services.

FISCAL IMPACT

This bill would not significantly impact departmental costs.

ECONOMIC IMPACT

Revenue Estimate

Based on limited data and assumptions below, it is projected that this bill would result in the following revenue losses under the B&CTL.

Estimated Revenue Impact of AB 684 As Amended 6/27/01 [\$ In Millions]		
2002-03	2003-04	2004-05
negligible loss	negligible loss	-\$0.5

Negligible loss is less than \$250,000.

Tax Revenue Discussion

The revenue impact of this bill would be determined by any future participation of credit unions in providing trust services that results in less income reported for tax purposes by other financial institutions.

To date, very few credit unions are in any way related with companies providing trust services. To the extent these few companies combine with a qualifying credit union, otherwise taxable net income from providing trust services would become tax-exempt under this proposal. Also, if additional qualifying credit unions engage in trust business and generate income from providing trust services that otherwise were provided by a taxable bank or trust company, additional revenue losses would result. As of year-end 1999, there were 687 federally chartered and state chartered credit unions in California with 8.5 million members.

It has been previously estimated that financial institutions currently providing trust services pay state income taxes on the order of \$30 million annually just on net income from fiduciary activities. Approximately 10%-20% of this tax revenue, or roughly \$5 million, is attributed to trusts with assets valued at \$1 million or less. Assuming such smaller trusts would be generally representative of the trust business potentially engaged in by qualifying credit unions, revenue losses of \$500,000 annually are projected after a number of years. Based on information in the California Statistical Abstract (2000), credit union assets are approximately 20% of commercial bank assets (insured commercial banks headquartered in California) at year-end 1999. For this analysis we are assuming that relative trust services income would be less, perhaps 10% of that of banks from smaller-valued trusts.

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